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NO. 89-1775

IN THE

Supreme Court of the United States

OCTOBER TERM, 1990

RICHARD HONGSERMEIER, FIDELA HONGSERMEIER, HOYT W. YOUNG, BARBARA D. YOUNG, ROBERT L. DUFRESNE, CAROLYN S. DUFRESNE, JERRY DIXON, PATRICIA DIXON, RALPH J. RINA, TERRY D. OWENS, AND GLORIA K. OWENS,
Petitioners,

v.

UNITED STATES OF AMERICA, ET AL,
Respondents.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

REPLY BRIEF FOR PETITIONERS

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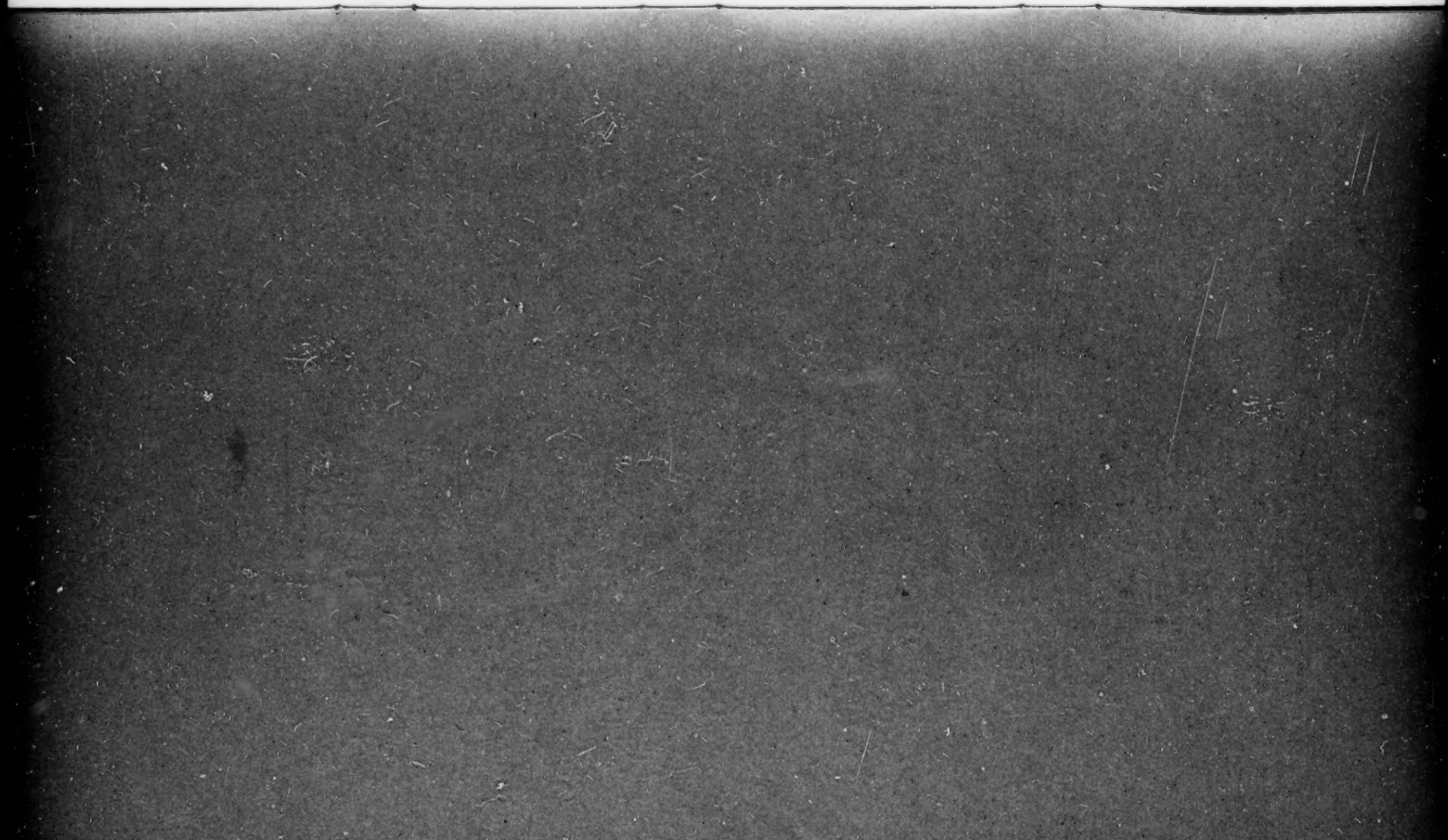

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To The Honorable Justices Of This Honorable Court:

Petitioners, Richard Hongersmeier, Fidela Hongsermeier, Hoyt W. Young, Barbara D. Young, Robert L. Dufresne, Carolyn S. Dufresne, Jerry Dixon, Patricia Dixon, Ralph J. Rina, Terry D. Owens, and Gloria K.

Owens (collectively "Intervenors"), submit this reply brief in response to the Brief in Opposition ("OPB. ____") filed herein by the United States of America ("Respondents" or "I.R.S.") on August 13, 1990. Petitioners incorporate by reference herein their Opening Petition and also reference, and join in the Opening and Reply Brief filed in No. 89-1775 by Petitioner Henry F.K. Kersting ("Petitioner").

STATEMENT

This case involves the issuance of a John Doe summons to Petitioner Kersting, for the records of investors in the so-called "Kersting companies," when the I.R.S. was aware of the identity of hundreds of persons whose records were summoned by the John Doe summons, including those of Intervenors, and was in possession of many of the documents summoned. The Government even continues its attacks on Petitioner Kersting, by attempting to smear him as a "promoter of tax shelters of questionable validity." Petitioners succinctly distinguish the Government's misrecital of *Pike v. Commissioner,* 78 T.C. 822 (1982).[1]

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1. *Pike* involved deductions for Sub-chapter S car leasing companies which were disallowed because the Tax Court found that there was no hope of making a profit because the car rentals were too low. It had nothing to do with the current companies with which Petitioner, Kersting is involved or was involved during the times relevant to the John Doe summons at issue in this case. The Government has attacked what it claims are "circular payments or exchanges of checks" and has further attacked the validity of the notes involved in financing the stock transactions in question (all the while acting through its agents to actively impede collection suits filed by the corporations in state courts). Indeed, the mere proof of circular payments or exchange of checks does not prove a sham and substantial economic interest may be involved, despite such check exchanges, which ultimately create bona fide indebtedness and result in substantial economic exchange of consideration. *United States v. Kilpatrick,* 726 F.Supp. 789 (D.C. Colo., 1989).

The Government next attempts to dismiss Petitioners' arguments in simplistic, albeit erroneous fashion.[2]

Despite their claims, Respondents essentially admit that the District Court should grant intervention, but only when they find jurisdiction to hear the claims raised following determination of the mootness issue after substantial compliance.

Despite its claim that Intervenors advance no argument to show the erroneous jurisdictional argument supported by the District Court and Appeals Court order, the Government fails even to address Intervenors' authorities supporting intervention. Respondents slyly back away from consideration of the law in *Gluck, supra.* Clearly if the Court followed *Gluck,* Intervenors could intervene in the summons enforcement action and participate in the hearings as they requested below.

Admittedly, the Government prevailed on the initial issue concerning administrative bad faith—the purpose of the investigation itself. The District Court, however, ignored procedure tainted by the Government's deliberate concealment of the known identities of 600 investors as well as its possession of literally hundreds of thousands of documents that responded to the John Doe summons. These facts fully reflect the Government's administrative

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2. Respondents oppose intervention because: (a) the District Court rejected intervention in the summons enforcement action below because the prior Notice of Appeal divested the court of jurisdiction, which the court of appeals affirmed on the same ground. OPB. 9-10; (b) Intervenors advance no authority or argument that suggest that this jurisdictional ruling was erroneous; and (c) No basis to disturb judgment below exists, and the merits of the intervention question is left to the district court on remand based on a determination that the case is not moot. *Id.;* 10 n.8.

bad faith in bringing the summons proceeding in the first instance, its "good faith affidavit" notwithstanding.

Only now does the Government admit the facts concealed from the lower courts. While they admit that the 600 investors discovered with the January 22, 1981 search warrant were then in Tax Court on some of the years in question in the summons, OPB. 2, the Government conveniently overlooks the fact that Intervenors were all parties in those same 1300 cases pending in the Tax Court litigation (*Dixon, et al v. Commissioner,* Docket No. 8392-83). The Government also neglects the "dragnet provisions" of the John Doe summons which had the effect of "capturing" documents going back to the first of January, 1981. If the I.R.S. was only interested in the investors in 1984-1986, why did it have to go back three more years and then conceal the documents which it already had in its possession?

This Court should note that the ultimate issues in *Dixon* involve the bona fides of the deductions generated through investments in the "Kersting companies." The same parties in this case litigated the issues in Dixon, as "Test Case petitioners," at the same time that the I.R.S. requested the John Doe summons for an allegedly separate investigation of the same or similar deductions.

In its Brief in Opposition, the Government blithely ignores the main issue on which Intervenors appealed—the Government's use of a John Doe summons when the identities of those whose records were sought were known to the Government and when many of the documents sought were already in the Government's possession. This all the while now admitting that the identities of 600 investors were known to the Government before the

summons was sought! This judicial admission of administrative bad faith was either blindly ignored by the District Court in its rush to compel Kersting to produce documents or concealed by the Government from the District Court in order to prevent it from reaching the proper conclusion on the Government's "good faith" in bringing the summons proceeding. As to the Intervenors, the Government admits that they "are among those investors currently engaged in litigation in Tax Court." (Brief in Opposition, page 5) Obviously, then the identities of these Intervenors and their participation in the "Kersting programs" was and is known to the Government because it is a matter of public record in the United States Tax Court—proceedings to which the Commissioner of Internal Revenue is a party.

The Government next makes an inconsistent argument. It claims the Court of Appeals for the Ninth Circuit affirmed on the ground (against the Intervenors) of lack of jurisdiction yet quotes early in its brief language of the Ninth Circuit which states that if Kersting has not substantially complied then the District Court is to take jurisdiction of the case and determine Intervenors' motions and grant Intervenors status to intervene.

The Government gravely misstates the holding of the Court of Appeals on the Motion to Intervene. Intervenors understanding of the Court of Appeals' ruling on the intervention was that it considered the claims of the Intervenors and noted that it was refusing to act because Kersting's turnover of his records "mooted" the controversy and that if the Government sought to use the records *then* the Intervenors could attack the constitutionality and legal propriety of the Government's use of

the John Doe summons procedure where the Intervenors' identities were known.

The Government's footnote #5 is inconsistent with its argument of lack of jurisdiction. The Government claims—

> "The Court of Appeals directed the District Court to determine on remand whether Kersting had substantially complied and, if it determined that a live controversy remains, to consider the merits of the motions previously denied by the District Court for lack of jurisdiction."
>
> See Brief in Opposition, Page 6, Note 5.

In essence, the Intervenors who were "locked out of the case" are now in the case if, as the Government claims, Kersting has not substantially complied with the summons enforcement order. Therefore, it would seem the Intervenors substantially prevailed on their appeal and were not "ruled against" by the Court of Appeals.

ARGUMENT

QUESTION I

THIS COURT SHOULD GRANT CERTIORARI TO DETERMINE WHETHER INTERVENORS MOTION TO INTERVENE SHOULD HAVE BEEN GRANTED.

Petitioner Kersting, in his related Petition for Writ of Certiorari and in his Reply Brief, sets out, at great length, the conflict in the Circuits on the mootness issue. Intervenors adopt Kersting's arguments and further assert that their interest as Intervenors in post-enforcement hearings under Title 26 U.S.C. Section 7609, including con-

tempt proceedings, and any subsequent appeal, is of equal weight and gravity as their position prior to enforcement.

A John Doe summons is a direction to a third-party to surrender information concerning taxpayers *whose identity is unknown* to the I.R.S. *See In Re Tax Liabilities of John Does,* 671 F.2d 977, 978 (6th Cir. 1982).[3]

> "Section 7609(f)'s criteria thus constitute a procedural safeguard which Congress created to provide extra protection to unknown target taxpayers to whom the I.R.S. cannot give notice."

United States v. Samuels, Kramer & Co., 712 F.2d 1342, 1346 (9th Cir. 1983), citing *United States v. Pittsburgh Trade Exchange, Inc.,* 644 F.2d 302, 305 (3rd Cir. 1981).

Intervenors had a specifically defined statutory interest which precluded I.R.S. utilization of John Doe summons proceedings with respect to their tax liabilities connected in any way to the "Kersting companies." The I.R.S. violated this statutory interest prior to the date of filing of Intervenors' Motion to Intervene. Intervenors thus had a statutorily created interest implicated by the proceedings below and, therefore, had standing to intervene irrespective of whether this Court ultimately determines Intervenors' intervention rights to be mandatory or permissive.

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3. Title 26 U.S.C. Sec. 7609 provides that the I.R.S. may serve such a summons only if it can establish in a court proceeding (1) that the summons relates to the investigation of a particular person or an ascertainable group or class; (2) that there is a reasonable basis for believing that such person or group or class of persons may fail or have failed to comply with any provision of any internal revenue law, and (3) the information sought to be obtained from the examination of records (and the identity of the person or persons with respect to whose liability the summons is issued) is not readily available from other sources.

Intervenors sought to assert this right to intervene before documents and information had been supplied by Kersting to the I.R.S. in response to the John Doe summons. Intervention was sought when Kersting was held in contempt and faced severe fines in the event Intervenors' records were not turned over. It was at this point that Kersting's representation of Intervenors' interests became ". . . inadequate. . . ." *Legal Aid Society of Alameda County v. Dunlap,* 618 P.2d 48 (9th Cir. 1980) at p. 50.

The compelling logic and rationale of *In Re: McElrath,* 248 F.2d 612 (D.C. Cir. 1957) addresses and rejects the mootness arguments advanced by the District Court, the Court of Appeals and the Government in its Brief in Opposition.

Even if this Court holds that this case would otherwise be moot, applying the "capable of repetition yet evading review" exception to the mootness doctrine recognized by this Court in *Southern Pacific Terminal Co. v. ICC,* 219 U.S. 498, 515 (1911), this Court should grant review because the latter prong of the exception—that the controversy be sufficiently likely to be repeated—has been met herein in light of the history of dealings between the parties and the increasing use of the John Doe summons by the I.R.S.

Since the *procedural irregularity* of I.R.S. use of John Doe summons procedures was squarely at issue and remained so throughout the pre-enforcement and post-enforcement summons proceedings, Intervenors should have been granted leave to intervene. The failure to grant such leave was error and should be reversed.

CONCLUSION

For the foregoing reasons, the petitions should be granted and a writ of certiorari should be issued to review the decision below.

Respectfully submitted,

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